

Leadership Conference on Civil Rights

1629 K Street, NW 10th Floor Washington, D.C. 20006

Phone: 202-466-3311 Fax: 202-466-3435 www.civilrights.org

STATEMENT OF WADE HENDERSON, PRESIDENT & CEO LEADERSHIP CONFERENCE ON CIVIL RIGHTS

"STRENGTHENING OUR ECONOMY: FORECLOSURE PREVENTION AND NEIGHBORHOOD PRESERVATION"

COMMITTEE ON BANKING, HOUSING, AND URBAN AFFAIRS UNITED STATES SENATE

JANUARY 31, 2008

Chairman Dodd, Ranking Member Shelby, and members of the Committee: I am Wade Henderson, President and CEO of the Leadership Conference on Civil Rights (LCCR). Thank you for the opportunity to testify in today's hearing on options for preventing foreclosure and preserving neighborhoods in the midst of a growing crisis in our nation's home mortgage lending system.

LCCR is the nation's oldest and most diverse coalition of civil rights organizations. Founded in 1950 by Arnold Aronson, A. Philip Randolph, and Roy Wilkins, the Leadership Conference seeks to further the goal of equality under law through legislative advocacy and public education. LCCR consists of approximately 200 national organizations representing persons of color, women, children, organized labor, persons with disabilities, the elderly, gays and lesbians, and major religious groups. I am privileged to represent the civil and human rights community in submitting testimony for the record to the Committee.

I would like to begin by explaining why the growing number of foreclosures is of such critical importance to LCCR and the communities we represent. Simply put, the right to the American Dream of homeownership has always been one of the most fundamental goals of the civil rights movement. It is vital because homeownership is the means by which most Americans build wealth and improve their own lives and the lives of their families, and homeownership is essential to the development of stable, healthy communities of which all Americans can be proud. For decades, the civil rights community has been struggling to not only break down the barriers to housing itself, but also to the credit that most Americans need to obtain housing. The resistance that racial and ethnic minority communities have faced in obtaining fair and sustainable mortgage loans, from the practice of redlining to the scourge of predatory lending, lies very much at the root of the crisis in which we now find ourselves today.

And indeed, after years of denial by many, there is a growing consensus that we do face a crisis. It is now finally well-accepted that the mortgage lending industry engaged in the widespread use of utterly reckless and predatory lending practices during the nationwide housing market "boom" that took place throughout much of this decade. While the use of *responsible* subprime lending could have created meaningful homeownership opportunities for people who might otherwise be



left out of the market, many homeowners were deceptively steered into expensive subprime mortgages even though they qualified for prime loans, with unreasonable terms and hidden fees that made it impossible for homeowners to stay current, much less get ahead – and there were clear, significant racial and ethnic disparities in the manner in which this was done.¹

To make things worse, many lenders – lured by the prospect of easy profits through the rise of securitization – took exotic practices such as "2/28s," "interest-only," "pay-option," "low-doc" or "no-doc" mortgages, prepayment penalties, and "yield spread premiums," and made them commonplace, abandoning sensible loan underwriting and appraisal standards in the process.²

The use of these sorts of practices, in housing markets that were bound to reach unsustainable peaks, guaranteed that millions of people would be unable to handle their monthly payments. Needless to say, too many families now see their American Dream slipping away – and it is profoundly disappointing to see that the end result of recent subprime lending practices is *less* homeownership, not more.³

As a steady stream of information about growing foreclosures⁴ and softening property values⁵ continues to flow in, and with growing uncertainties about our economy, it is clear that Congress must take a swift, pragmatic, multifaceted approach to restore homeowner confidence and preserve the communities that we have all worked so hard to develop. At the same time, I am

¹ See, e.g. Debbie Gruenstein Bocian, Keith S. Ernst, and Wei Li, Unfair Lending: The Effect of Race and Ethnicity on the Price of Subprime Mortgages, at 19 (available at

http://www.responsiblelending.org/pdfs/rr011-Unfair_Lending-0506.pdf), May 2006; National Community Reinvestment Coalition, *Income is No Shield Against Racial Differences in Lending: A Comparison of High-Cost Lending in America's Metropolitan Areas* (available at

http://ncrc.org/pressandpubs/documents/NCRC%20metro%20study%20race%20and%20income%20disparity%20July%2007.pdf), July 10, 2007; Rich Brooks and Ruth Simon, "Subprime Debacle Traps Even Very Credit-Worthy," *Wall Street Journal*, December 3, 2007 at A1.

² See, e.g. Comptroller of the Currency John C. Dugan, sharply criticizing widespread use of "no/low-doc" loans:

Sound underwriting – and, for that matter, simple common sense – suggests that a mortgage lender would almost always want to verify the income of a riskier subprime borrower to make sure that he or she had the means to make the required monthly payments. But the norm appears to be just the opposite: nearly 50 percent of all subprime loans last year accepted stated income. . . . I do find it telling that, when faced with new housing market conditions, lenders have responded first by tightening standards on stated income. . . . Apparently verified income is viewed as a critical factor in determining whether a loan can be saved, which of course begs the question: if loan verification is such an important predictor of the borrower's ability to repay in the current environment, why wasn't it equally important when the loan was first made?

News Release: "Comptroller Dugan Expresses Concern Over 'Stated Income' Subprime Loans," *Comptroller of the Currency*, May 23, 2007, available at http://www.occ.gov/ftp/release/2007-48.htm.

³ Center for Responsible Lending, "Subprime Lending is a Net Drain on Homeownership," CRL Issue Paper No. 14 (March 27, 2007).

⁴ See, e.g. Press Release: "U.S. Foreclosure Activity Increases 75 Percent in 2007: More Than 2.2 Million Foreclosure Filings on Nearly 1.3 Million Properties Reported," RealtyTrac, Jan. 29, 2008, at http://www.realtytrac.com/ContentManagement/pressrelease.aspx?ChannelID=9&ItemID=3988&accnt=64847 (accessed Jan. 30, 2008).

⁵ See, e.g. Michael M. Grynbaum, "Home Prices Sank in 2007, and Buyers Hid," *The New York Times*, Jan. 25, 2008; "Bloomberg News, "S.& P. Home Price Index Continued to Fall in November," Jan. 30, 2008, at http://www.nytimes.com/2008/01/30/business/30home.html.



mindful of the concerns that many have raised - particularly in light of the looming fears of difficult economic times ahead – about the need to avoid steps that saddle future generations with additional debt, increase the costs of credit, or resort to "bailouts" that might encourage more irresponsible mortgage finance practices in the future.

The Administration – and as I am pleased to note, the lending industry as well – has already taken one very significant step in addressing the current foreclosure epidemic. The so-called "Paulson Plan" and the related "Hope Now Alliance" in particular, and voluntary industry-based efforts in general, rightly deserve praise. Every home that is saved from foreclosure is a step in the right direction.

But it is clear, from the lending industry's own numbers, that voluntary efforts are far from sufficient.⁶ Only three percent of subprime adjustable rate mortgages will be eligible for relief under the Paulson Plan.⁷ When I testified in a House Judiciary Committee hearing this Tuesday, 8 a fellow witness and friend, Ms. Faith Schwartz of the Hope Now Alliance, acknowledged during questioning that voluntary efforts were indeed not going to save every homeowner, and I appreciated her candor and agreed with her observation. The importance of preserving homeownership, to our communities and to our nation, demands that more be done. With that in mind, I strongly urge this Committee and Congress to quickly move forward on several additional, important steps.

Moratorium on Foreclosures, Revisited

Last spring, Mr. Chairman, following a series of discussions that you convened with leaders of the lending industry and stakeholder organizations, the civil rights community proposed the idea of a voluntary, industry-led moratorium on subprime mortgage foreclosures. We believe that such a moratorium would give the industry time, before the irreparable damage of more foreclosures occur, to work actively with homeowners to help them keep their homes by providing more affordable loan products. While I am mindful that some borrowers utilized subprime loans in an effort to reap profits during the recent real estate boom, as opposed to borrowers who simply wanted to own homes in which they and their families could live, we argued that a moratorium would provide the time needed to find and assist borrowers who truly deserve help.

While we were relieved that a number of major originators and servicers of subprime loans at least took the time to respond to our call for a moratorium, unfortunately, the nature of those responses was underwhelming. Those who responded said that they wanted to minimize foreclosures, and I had no reason to doubt their sincerity, but it was very clear to me from their correspondence that a comprehensive, industry-wide effort to do so had not yet taken shape.

⁶ Mortgage Bankers Association, "An Examination of Mortgage Foreclosures, Modifications, Repayment Plans, and Other Loss Mitigation Activities in the Third Quarter of 2007," Jan. 2008, at 22.

⁷ Center for Responsible Lending, "Voluntary Loan Modifications Fall Far Short," CRL Issue Brief, Jan. 28, 2008.

⁸ Hearing: "The Growing Mortgage Foreclosure Crisis: Identifying Solutions and Dispelling Myths," U.S. House, Committee on the Judiciary, Subcommittee on Commercial and Administrative Law, Jan. 29, 2008.



While I do not dispute that the industry has been making progress in developing more widespread foreclosure avoidance efforts since we called for a moratorium, it is also clear that the extremely complicated nature of mortgage securitization structures that developed in recent years pose a major challenge to the success of those efforts. Potential conflicts between primary and junior mortgage liens also raise difficulties in many cases. 10

Given these difficulties, and the still-unacceptably high number of foreclosures that have been taking place to date despite the efforts of many in the industry, ¹¹ I believe that the idea of a foreclosure moratorium should be revisited. Indeed, I believe that this Committee should explore ways in which it could mandate one, in order to circumvent the barriers that make a voluntary one unlikely. While I realize that this would be a drastic measure, we are clearly facing a situation in the housing market and the economy unlike any other in recent history. A forced "cooling off" period could give the industry time to further develop its own solutions, and greatly ease public concerns about the devastating toll that the growing number of foreclosures is taking on our economy.

Bankruptcy Reform: Chapter 13 Relief

Even if a foreclosure moratorium provides more time to further develop industry-led efforts, it is indisputable that those efforts alone will not help every deserving homeowner. And while I recognize that matters involving bankruptcy law lie outside of the jurisdiction of this Committee, I believe that proposals to allow borrowers to seek relief in Chapter 13 bankruptcy proceedings are worth briefly discussing in the context of today's hearing.

Certainly, Mr. Chairman, as a cosponsor of Senator Durbin's bill, the "Helping Families Save Their Homes in Bankruptcy Act of 2007" (S. 2136), you are already well aware of the merits of this approach. But I would like to encourage each of your colleagues on the Committee to join you in this effort, if they have not done so already. LCCR strongly believes that Chapter 13 reform is one of the most important policy options available to Congress in the effort to reduce the number of foreclosures.

A proposal like S. 2136 would give literally hundreds of thousands of borrowers who are in danger of foreclosure a chance to save their homes through the use of bankruptcy proceedings. It would enable bankruptcy courts to: 1) reduce the principal owed on a subprime or non-traditional mortgage to reflect the actual value of the home; 2) reset interest rates to affordable-but-fair levels; and 3) eliminate prepayment penalties and other abusive fees.

There are several major benefits to this approach. One key advantage is its cost. Because bankruptcy proceedings would not involve the use of public funds, it would not give the appearance of a "bailout" or raise moral hazard issues. Indeed, for people who want to utilize

¹¹ Supra note 6.

⁹ See, e.g. Center for Responsible Lending, supra note 6; Testimony of Kurt Eggert, Hearing: "Subprime Mortgage Market Turmoil: Examining the Role of Securitization," U.S. Senate Subcommittee on Securities, Insurance, and Investments, Apr. 17, 2007 at 19-26.

¹⁰ *Ibid*.

¹² I am very grateful to Senators Brown, Menendez, Reed, and Schumer for also cosponsoring S. 2136, and to several additional Senators not on this Committee.

bankruptcy laws to save their homes from foreclosure, it will still come at a heavy enough cost – monetary and otherwise – to encourage wiser financial decisions in the future.

At the same time, such an approach would clearly benefit not just individual homeowners who cannot be adequately helped by industry-led efforts, but the entire public and our economy at large. Every home that gets saved from foreclosure – by any means – helps to protect the value of the homes surrounding it from unnecessary declines, meaning that other homeowners will be less likely to get "upside down" on their own mortgages and possibly face foreclosure as well.

I am all too aware that the mortgage lending industry has voiced strong opposition to this bill. In particular, opponents argue that it would substantially raise the risk of mortgage losses, and therefore raise the cost of future loans. While I take such concerns very seriously, I am not convinced that those fears are warranted with respect to S. 2136 as it is written. Indeed, I believe that it is a wise and long-overdue change to our bankruptcy laws.

On Tuesday, however, I testified before the House Subcommittee on Commercial and Administrative Law in strong favor of a greatly-modified version of H.R. 3609, the "Emergency Home Ownership and Mortgage Equity Protection Act of 2007." In an effort to address even the *potential* risk that H.R. 3609 might adversely impact the costs of mortgage loans in the future, Chairman John Conyers and Representative Steve Chabot crafted a very thoughtful compromise that, in the opinion of a majority of the witnesses in Tuesday's hearing, eliminates those risks beyond a shadow of a doubt. In particular, the Conyers-Chabot compromise would apply only to subprime and non-traditional mortgages that were originated between January 1, 2000 and the date of enactment, and would sunset in seven years. While I still believe that permanent changes to Chapter 13 are warranted, the Conyers-Chabot substitute would certainly be an acceptable approach for dealing with the mortgage crisis that we are facing here and now.

Additional Good Ideas: "Federal Homeownership Preservation Corporation" and "Great American Dream Neighborhood Stabilization Fund"

Naturally, because of the tremendous toll that it inflicts on a borrower, the Chapter 13 bankruptcy relief I discussed above must always serve as a last resort. With that in mind, and while several of my fellow panelists will discuss them in much greater detail, I want to briefly touch on two additional proposals fro the Center for American Progress that I am happy to see are under discussion today and that I am pleased to support as additional ways to deal with our foreclosure epidemic.

The proposed "Federal Homeownership Preservation Corporation" (FHPC) is a welcome throwback to the Home Owners Loan Corporation (HOLC), a New Deal-era program that saved nearly one million homes from foreclosure during the Great Depression of the 1930s. Like the HOLC, Senator Dodd's proposal would facilitate the purchase of troubled pools of mortgage-backed securities at a substantial discount from investors, and leverage existing institutions' capacity to quickly replace the underlying mortgages with newly originated loans to homeowners at fair market values and reasonable fixed rates.



This idea worked in the 1930s, and I believe it can work in 2008 as well. It could spare a great number of homeowners from foreclosure, put the losses where they belong, and be not just costneutral to the public but even profitable. At the same time, it would allow home prices to correct without – unlike foreclosures or abandonment – letting them crash through the floor.

Another important proposal, named the "Great American Dream Neighborhood Stabilization Fund" ("GARDNS") would address the problem of homes that are already vacant. It would create grant funds to allow community land trusts, community development corporations, or similar entities to purchase foreclosed or REO ("real estate owned") homes in troubled areas at substantial discount, and sell them to low- or moderate-income buyers while retaining a share of the value. The initial grant moneys could be leveraged several times over as the proceeds from each sale would flow back into the fund to allow for new REO acquisitions. Like the FHPC, the GARDNS proposal carries with it the added benefit of already having been proven to work.

Conclusion

I believe the use of responsible, sustainable subprime lending practices *can* expand home ownership and, at the same time, prove rewarding to investors. But the idea of subprime lending went terribly astray in recent years. And with a foreclosure crisis unlike anything we have seen in decades, homeowners – and our economy as a whole – simply cannot afford to wait for an industry that collectively created the mess, and is now being devoured by it, to take the lead in cleaning it up. I want to thank you for your leadership and for holding this hearing on more comprehensive action, and I look forward to any questions you may have.